Analysis: Common Framework, familiar problems: hopes of debt breakthrough fade

By **Libby George**

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Chinese yuan banknotes are seen in this illustration picture taken April 25, 2022. REUTERS/Florence Lo/Illustration

LONDON, June 20 (Reuters) - Cautious optimism in the developing world that wealthier countries and China had finally fixed the tortuous process of sovereign debt restructurings is fizzling again.

Debt crisis veterans gave a weary thumbs up in April to plans to galvanize the G20-led "Common Framework" - a platform supposed to speed up and simplify the process of getting overstretched countries back on their feet.

Though Zambia, locked in default for almost three years, does look to be making some progress, many of the thorny issues that have drawn criticism of the Common Framework remain.

One is how China, now the largest bilateral lender to the developing world, swallows losses. Another is how much debt poorer countries can carry given ultra-low global interest rates are a thing of the past.

The result is that countries trying to restructure their problematic debt have been left to negotiate bespoke arrangements in much the same way they did in the past.

"There was optimism that a deal could be clinched relatively quickly," said Cornell University professor and former head of the IMF's China Division Eswar Prasad, referring to the April reboot of the Common Framework. "That optimism proved unwarranted."

Even news that Zambia's public creditors are prepared to make a debt restructuring proposal, after the country had resorted to public pleas for urgency, was "unlikely by itself to signal a breakthrough in negotiations on urgency, was "unlikely by itself to signal a breakthrough in negotiations on the broader framework for debt restructuring," Prasad said.

G20 nations launched the 'Common Framework' in 2020, when the COVID pandemic upended nations' finances. Nearly three years later, with Zambia, Chad, Ethiopia and Ghana all in the set-up, it is yet to chalk up a solid success.

The core struggle has been how much debt countries need to write off, and coaxing China, after a decade-long lending spree, into debt talks that it views as designed by western powers.

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The April attempt **to reform** the Framework saw the IMF promise to share more information earlier, particularly regarding debt sustainability, and to give struggling countries more concessional finance.

In exchange, the hope was that China would back down from demands that multilateral lenders relax their "preferred creditor status" and take loan losses.

Others said it was far from clear that China had abandoned some of its tough requests, including that multilateral development banks take loan losses.

Neither the People's Bank of China nor China's Finance Ministry immediately responded to requests for comment. In April, China said it was willing to work with all parties on the Common Framework but it has not commented publicly on the issue since then.

"There was a bit of misreporting about a breakthrough," said Kevin Gallagher, director of the Boston University Global Development Policy Center, adding there are also questions about how much concessional lending multilateral development banks can give.

In a note earlier this month, analysts at JPMorgan said that despite "incremental changes" to the Common Framework, the core tensions remained, making debtor countries subject to it more reluctant to "preemptively pull the trigger" on restructuring.

They estimate that the government bonds of 21 countries, with a combined value of $240 billion, are now at "distressed" prices.

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CREDITOR CLASHES

Bringing China into the fold of the traditional Western-led "Paris Club" of creditor nations, and the "London Club" of private creditors like pension and hedge funds, has prompted enormous challenges.

That high-profile friction has seen even U.S. Treasury Secretary Janet Yellen **publicly accuse** China of being a roadblock to deals.

This has amplified fiscal pain for countries like Zambia, which has been in default since 2020.

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"I think they are all slightly fed up as they feel they're getting trampled on -- caught between a broader battle," said Thys Louw, portfolio manager for emerging markets with Ninety One.

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Beijing issued some $138 billion in new loans between 2010 and 2021, according to the World Bank, making its sign-off essential as a condition to unlock IMF funds. Zambia owes China some $5.9 billion, roughly 23% of its GDP and close to half of the $12.8 billion of the external debt it is trying to restructure.

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Zambia even asked French President Emmanuel Macron to **use his clout** to help.

'TANGIBLE' PROGRESS

The IMF, World Bank and the G20 created the Global Sovereign Debt Roundtable (GSDR) early this year to fix the Framework and speed debt restructurings.

The IMF said this month it expects "tangible" progress during June GSDR meetings.

Louw said Ghana's relatively speedy IMF staff-level agreement, and Zambia's forward momentum were positive signs.

"I do think we're much closer now to understanding what's required from everyone in the room," Louw said.

But until a widely accepted framework is in place, indebted nations are stuck in uncharted waters, slogging through each piece of their debt deals individually. And observers note that Ghana still faces the bigger hurdle of getting creditors to agree on new terms.

"Very often people involved in these discussions let their optimism get ahead of the facts...and then once it comes down to brass tax, when people look at who's going to take how much of a haircut, things start falling apart," Prasad said.

"I think it's just going to be a grinding negotiation."

Additional reporting by Joe Cash in Beijing. Editing by Marc Jones and Christina Fincher

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